LOS ANGELES COUNTY
ISD

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To enrich lives through effective and caring service.

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May 19, 2004

To: Each Supervisor

From: Dave Lambertson
Interim Director

Subject: **ENERGY UPDATE REPORT**

ISD periodically updates your Board on the County's ongoing energy management activities. This update provides status on the County's settlement with El Paso Corporation, the California Public Utility Commission's (CPUC's) $3.7 million award to the County for energy projects, new energy legislation under proposal for California and a proposed liquefied natural gas terminal in Long Beach.

Natural Gas Settlement with El Paso Corporation (El Paso)

As reported in previous Energy Update Reports, the County and El Paso entered into a settlement agreement to resolve the County's claims and lawsuits against El Paso related to the sale and delivery of natural gas. Under the terms of the settlement agreement, El Paso agreed to pay the County an upfront payment of $9,168,170 and had the option to either:

- Make 40 semiannual payments of $223,593 (total of $8,943,713), or

  Prepay the deferred payments at a discounted present value amount.

El Paso has elected to prepay the deferred payments at a discounted present value amount of $4,521,544. This, combined with the $9,168,170 prepayment brings the County's total gross recovery under the settlement to $13,689,714. The County's gross recovery will be reduced by attorneys' fees and costs payable to our contract counsel. These costs are estimated to be $2,223,457 resulting in proceeds to the County of $11,466,257.

It is currently estimated that the County will receive its recovery under the El Paso settlement in June of 2004.

CPUC Energy Efficiency Program – Joint County/SCE/SoCalGas Award

In our prior Energy Updates, ISD reported we were seeking CPUC's final approval for a $3.7 million award to the County as part of a partnership proposal by ISD, Southern California Edison (SCE), and the Southern California Gas Company (SoCalGas). The award has been approved by the CPUC as part of their Public Goods Charge Energy Efficiency Funding Program for calendar years 2004 and 2005. This program is designed to provide funding to utilities and non-utilities for worthwhile energy projects.

The CPUC's instructions for the 2004-05 Program strongly encouraged third parties, and especially local governments, to form partnerships with Utility Companies in an effort to maximize outreach and energy savings and minimize administration costs. The CPUC's criteria for evaluating the more than 400 proposals they received included cost effectiveness and long-term energy savings, peak demand reductions, ability to reach traditionally neglected markets, innovation and coordination with other entities. The Program will include the following initiatives:

Building Retro-commissioning – Retro-commissioning essentially involves the tune-up and repair of building energy systems (i.e., air conditioning, etc.). Increasing the efficiency of these systems results in energy savings. The program will include $2.5 million of building retro-commission projects, yielding annual energy savings of approximately $400,000.

CDC Projects – ISD coordinated with the Community Development Commission/ Housing Authority in an effort to show how these entities could work together in implementing innovative projects in what the CPUC recognizes is a "hard to reach" market. Under the direction of SCE and a contractor, information devices that indicate real time energy consumption data and energy budget projections will be provided to public housing residents who pay their own utility bills. Theoretically, this would assist residents in lowering their energy costs. ISD will also help facilitate SCE's other low income housing energy efficiency rebate programs at CDC/Housing Authority facilities.

- Regional Efforts – ISD/SCE/SoCalGas will conduct a study of how to improve the administration and implementation of energy efficiency throughout the Southern California region on behalf of various local public agencies and governments. In the past, ISD has communicated with the County Office of Small Business, the County Office of Education, the Community Development Commission and the Metropolitan Transit Authority on energy issues. ISD has discussed energy policies with various local governments including the Southern California Cities Joint Powers Consortium. The CPUC recognizes that groups of local governments, public agency alliances and other natural collaborations could be more effective in developing and implementing energy programs.

- Recently, these types of studies have led to the creation of regional energy offices serving Ventura County, Humboldt County and San Diego County. They are all Joint Powers Agencies created to develop and implement sustainable energy policies within each region. The Ventura County and Humboldt County Regional Energy Alliances were created in 2002 using CPUC program funding. The San Diego Regional Energy Office has been in existence for nearly 10 years and is funded through grants from various regulatory agencies.

In the near future, ISD will be submitting a Board letter requesting authority for ISD's Interim Director to enter into an agreement with SCE and SoCalGas to implement the program for 2004-05 under the CPUC's program guidelines.

Energy Legislation

There are over two dozen energy bills being considered by this legislature. However, three of them best reflect the positions of most interests in the State: re-instituting some form of customer choice (deregulation) and moving the utility industry back to a system of regulated utility monopolies. The three bills are summarized below:

<u>AB2006 (Nunez)</u>

AB2006 is supported by SCE. The bill, which is currently scheduled for consideration in the Assembly Floor, would allow for some customer choice beginning in 2005. Large customers (greater than 500kW demand) would have the opportunity to buy energy from third parties. This would include the County's 40 largest accounts in SCE territory representing nearly half of the County's total payments to SCE. The bill would also put SCE back into the power plant business by allowing them to invest in generation resources to secure reliable supplies for customers they serve as well as entering into long-term contracts with other generators.

Opponents of the AB2006, The Utility Reform Network (TURN), third party energy providers and power plant developers, claim that SCE would be given unfair advantage in developing generation resources because SCE's energy investments would be guaranteed fixed returns and SCE's customer base would remain relatively stable. Conversely, third party project developers and marketers would be subject to competitive market risks.

The California Chamber of Commerce supports AB2006. The other investor owned utilities and the State's municipal utilities have not taken a position on the bill. They will likely fight to have certain language amended in the bill.

The CPUC is split on the bill. The CPUC's President, Michael Peevey, supports customer choice as early as 2005 but would like to see amendments in AB2006 to ease the transition back to customer choice. Conversely, the CPUC's Energy Division report on deregulation proposes delaying customer choice until no sooner than 2009. This report has been criticized by President Peevey for being too timid on supporting competitive markets.

<u>AB428 (Richman)</u>

This bill was introduced in the last legislative session, died in Committee, but was granted reconsideration. It is similar to AB2006 in allowing choice only for large customers. AB428 will not grant SCE the authority to obtain generation assets to meet its load requirements. SCE would have to purchase or contract for power from a competitive power supply market. Third party energy suppliers and power plant developers support this bill. AB428 is thought to have little or no chance of passing.

<u>SB888 (Dunn)</u>

This bill did not pass in Assembly in the last legislative session but was granted reconsideration. SB888 would completely do away with deregulation by repealing AB1870, the original deregulation legislation. SB888 is thought to have little or no chance of passing.

<u>Next Steps</u>

The County's legislative analysts believe that if any energy legislation is passed this year it will be a modified version of AB2006. Given this, ISD and the CAO's legislative group will track the bill and propose amended language as necessary. ISD will likely propose specific language changes to protect the County's interests in customer choice, in pursuing the feasibility of being a Community Choice Aggregator, or in supplying the County's facilities from its own generation sites like Civic Center and Pitchess cogeneration plants.

Rate Activities

There have been several recent developments related to utility rates.

SCE's Proposed Economic Development Rate (EDR)

On April 6, 2004 SCE announced a proposed new rate structure at the CPUC aimed at promoting business expansion in California by providing rate incentives to help businesses expand within or relocate to the State. The EDR would provide 5-year rate discounts to medium sized businesses that meet certain financial criteria. The EDR would provide a 25% reduction for businesses in the first year of a 5-year contract; the discount would decline by 5% each year through the remaining years of the contract.

Customers may qualify for the EDR if they have at least a 200kW demand and can demonstrate that "but for" the rate incentives, they would not start, expand or retain business in California. Businesses outside of California qualify for the EDR if they can show that "but for" the rate incentives they would not relocate in California. The EDR is not available to state and local governments and retail establishments. The qualifying requirements must be approved by the CPUC and will be strictly monitored by SCE.

SCE has modeled the EDR after similar programs authorized by the CPUC in 1996 and 1998. Between 1996 and 2000 under those programs, SCE signed contracts with 66 businesses that eventually remained in the State, expanded, or relocated to the State. Those programs expired in 2000.

Although the County's facilities do not qualify for the EDR, the County benefits from the retention and creation of jobs in SCE territory under the program. ISD will monitor this proceeding and report to your Board on the implementation and results of SCE's EDR program.

Water Rate Increase

A plan to raise the Department of Water & Power's (DWP) water rates by 11% this year was backed by the City Council's Commerce, Energy and Natural Resources Committee on April 27, 2004. At the same time, DWP also indicated that water rates must increase by an additional 21.5% over the next four years to pay for improvements to their water system infrastructure and to implement terrorist protection measures.

For water accounts managed by ISD, the impact of an 11% increase in DWP water rates is estimated to be $0.7 million per year. ISD's managed water utility budget for FY 2004-05 already incorporates sufficient funds to cover the rate increase. This budget does not include water utilities for Public Works and Parks and Recreation.

SCE General Rate Case

SCE's General Rate Case is ongoing. The status has been reported to your Board in the previous energy update reports. In this proceeding, SCE has requested an increase in their annual revenues to cover increased operating, maintenance and business costs – primarily in their transmission system. The proceeding will determine the allocation of this increase from various customer classes. The amount of SCE's proposed annual increase and the proposed allocation of the increase among customer classes have not changed since described in the last Energy Update Report dated December 30, 2003. Any new rates approved by the CPUC will not go into effect earlier than August 1, 2004.

Community Choice Aggregation (CCA)

The County continues to participate in this proceeding at the CPUC, which will establish the rules and regulations for CCA. CCA allows local governments, cities and counties (Aggregators) to purchase and sell electricity on behalf of utility customers in their jurisdictions. Aggregators may also receive funding to implement energy programs.

A pilot study is being conducted by Navigant Consulting, Inc. and is partially funded by a grant from the Local Government Commission. The pilot study will assess the cost feasibility of CCA and is being conducted for the County's own facilities as a proposed "phase-in" of CCA. The County's unincorporated area ratepayers are also included in the pilot study. The CPUC proceeding will conclude later this Fall. At that time the County's pilot study will determine whether it is economically feasible to continue assessing CCA.

Liquefied Natural Gas (LNG) Plant Proposed in Long Beach

Several LNG plants have been proposed for development in California. Safety concerns raised by local residents have caused proposed project plans in Eureka and Vallejo to be abandoned. Proposed plants are still being considered in Long Beach and offshore of Ventura and Santa Barbara. An additional project is proceeding offshore of Baja California. Although ISD does not have a formal role in LNG, we have developed a fact sheet on the Long Bach Plant as well as general information on LNG (attached).

If you have any questions, please contact me or have your staff contact ISD's Energy Management Division Manager, Howard Choy, at (323) 881-3939.

DL:HWC:lf
Attachment
c: Chief Administrative Officer
Each Department Head
County Counsel

FACT SHEET

LONG BEACH LNG PROJECT STATUS

The Long Beach project has been proposed by Sound Energy Solutions (SES), a subsidiary of Mitsubishi Corp. In January of 2004, SES filed for a permit at the Federal Energy Regulatory Commission (FERC) to construct the project in Long Beach. The CPUC had requested SES to file for a permit at the CPUC claiming that California has statutory jurisdiction to permit the facility. In April of this year, FERC ruled that SES did not have to file with the CPUC and that siting, construction and operation of the facility fell under federal jurisdiction only.

FERC is working with the Port of Long Beach (Port) on a joint, environmental analysis of the project with the Port acting as the lead agency under the California Environmental Quality Act (CEQA). FERC is also conducting an environmental review as required by the National Environmental Policy Act (NEPA). These environmental studies will consider potential impacts on the environment and cultural resources directly related to tanker operation, marine facilities operation, proposed safety measures and terminal site construction and operation.

The battle over permitting jurisdiction has been elevated. In April of this year, the CPUC issued an Order Instituting Investigation (OII) into SES's proposal to construct and operate the Long Beach project. The CPUC maintains that California has a compelling interest in the siting, construction and operation of the project and retains the authority to issue permits for natural gas facilities in order to protect State residents from potential environmental and safety hazards. Additionally, the CPUC's OII claims that SES's proposal to sell converted LNG into the State's natural gas market would make SES a public utility and therefore subject to existing CPUC Code.

The OII names SES as a proceeding respondent and requires them to apply for necessary CPUC certifications to construct the project and to submit to all information requests by the CPUC and other interested parties. A pre-hearing conference will be set to establish the procedural schedule.

Description of LNG Technical Features and the Long Beach Project

Natural gas is a vapor at normal temperatures and liquefies at minus 256 degrees Fahrenheit. When natural gas is liquefied it takes up one-six hundredth of the volume of its gas form. LNG does not need to be stored under pressure so it is relatively easy to transport. As a liquid, natural gas is not flammable. Natural gas vapor burns when exposed to an ignition source; however, it is only flammable when the ratio of gas to air is between 5 and 15%. Above or below that range, the vapor will not burn. If LNG is exposed to normal temperatures, it will immediately vaporize. If spilled in water, LNG will rise to the surface and vaporize.

LNG can be offloaded from tankers at ocean sites (typically converted oil derricks) located several miles offshore, stored as liquid and converted to gas there, and then piped onshore. LNG is also delivered from tankers directly to onshore storage tanks, converted to gas and then piped into the utility pipeline system. The onshore design is proposed for Long Beach.

The project in Long Beach would cover 27 acres, cost $400 million and includes an offloading dock located onshore in the Long Beach Port. The project also includes two, 5.6 million cubic feet LNG storage tanks and facilities to convert LNG back to gas. The plant would produce an average of 600 million cubic feet per day of natural gas that would be delivered to customers through the SoCalGas intrastate pipeline system. A pipeline would have to be built connecting the facility with the pipeline system. The facility would be operational by 2007 or 2008.

General Pros and Cons

The LNG facility is anticipated to provide several million dollars per year in revenue for the Port of Long Beach. The City of Long Beach will also receive several million dollars per year from a new natural gas delivery pipeline. Additionally, the daily volume of natural gas produced by the facility is approximately 10% of the daily need in the entire Los Angeles region. Because the LNG is delivered through the Port, and not through the intrastate gas pipeline delivery system, typical pipeline transmission capacity and congestion problems are not a factor in delivering gas into California. This volume of natural gas delivered into Long Beach should help lower natural gas prices for customers in Southern California. Industry experts believe that LNG can be produced and delivered into Southern California for between $2 to $3 per MMBtu. Current natural gas prices are near $5.50 per MMBtu and have spiked as high as $50 per MMBtu during 2001. Projected high natural gas prices over the next 4-5 years reflect dwindling resources and the uncertainty of LNG as a viable market supply.

LNG facilities have been in operation in the United States for over 60 years. Most of the 113 LNG facilities in the United States are on the East Coast. A natural gas liquefaction facility in Alaska was built in the 1970's and is used to export LNG to Japan. The most serious LNG facility accident in the United States occurred in 1944, in Cleveland, when a storage tank failure led to a release of LNG that vaporized and ignited, killing 128 people. The most recent accident in the United States involved an explosion in Maryland in 1979 that killed one person and injured one person. In January of this year, an explosion at liquefaction and shipping terminal in Algeria killed 27 people and injured dozens.

The proposed LNG projects in Eureka and Vallejo were abandoned over safety concerns raised by representatives of those communities. The safety concerns included potential explosions and fires due to leaks and flammability and the increased threat of terrorist attacks on LNG sites. A particular concern for the Long Beach project, as raised by some local representatives at FERC, is the perceived lack of thoroughness in the permitting process at FERC. Outside of the FERC permitting process, the only other risk analyses planned for the Long Beach project will be conducted by SES and the Port of Long Beach. Additional concerns relative to the Long Beach project have been raised because of the seismic activity around the area and the proximity of heavily populated residential areas.

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f: Long Beach LNG – Fact Sheet (5-17-04)